

MISSOURI DEPARTMENT OF ECONOMIC DEVELOPMENT

DIVISION OF CREDIT UNIONS

NEWSLETTER

Volume 6, Number 6

April 29, 2004

INTEREST RATE ENVIRONMENT

Recent comments by the Federal Reserve and certain economic conditions seem to indicate interest rates could begin to increase within the next six months. The fact the discount rate is now at a 45 year low also increases the probability of a rate hike. Once interest rates begin to move the question becomes how far will they rise and how fast will it happen. Credit union's response to this question is critical to providing the best service to members and sound asset/liability management.

Although there are many considerations in pricing shares and loans credit unions must make adjustments to match market conditions. Credit unions should know under what circumstances that certain rates would almost be automatically adjusted. Many credit unions already are familiar with this concept as money market and variable rate loans are re-priced according to an index.

Adjusting dividend and loan rates on a timely basis is critical to success. Much can be said for making these decisions on pricing at least as often as when the Federal Reserve adjusts rates. Failure to adjust rates on a timely basis becomes more critical depending on how quickly and how far rates increase.

Many credit unions failed to adjust rates on a timely basis during the most recent decrease. The result was they attracted deposits at a higher cost than they could effectively use, loans decreased because members could find less expensive financing and net margins decreased. It is likely the opposite effect will take place as rates rise if credit unions do not adjust rates in response to market conditions. One additional concern in this scenario is liquidity.

Credit unions should establish procedures so they know when and under what circumstances action must be taken on decisions regarding pricing of shares and loans.

LENDING

Return Analysis-

Sound financial management requires a routine analysis of the return on the loan portfolio. At least three areas need to be reviewed:

1) Risk Based Pricing

Be sure to review each risk level to determine profitability. To gauge whether each tier is profitable, management must be able to identify the loans within that tier. Use of a designated field to record the grade of paper will facilitate the financial analysis.

Tracking of delinquency and net charge offs per grade of paper can then be factored into the profitability of each tier. This enables management to review the scores for each particular tier and determine that the pricing is appropriate.

2) Credit Card Portfolios

A recent article in a trade publication noted that 100 credit unions across the country have sold their credit card portfolios. Within Missouri, at least five credit unions have sold their portfolios.

Determining whether or not to hold your credit card portfolio is an individual decision. However, several credit unions have obviously decided that this program is not providing an adequate return. If you haven't reviewed your program within the past twelve months, it is time for an analysis. Consideration must be given to many factors, including net charge offs, staff time, and other indirect costs. If the program is not profitable, you may wish to sell the portfolio or provide the service through alternative means.

3) Vendor Reviews

Some products have profitability studies performed by the vendor providing the product. Regardless of the product, credit union management must be suspect of profitability reviews performed by the party making a profit from the sale of the item. It is difficult for these reviews to be objective.

One specific case is the review of Centrix loans. To properly determine the profitability of the portfolio, management should not rely on the vendor. Rather, management should pick a pool of loans granted within a relatively short timeframe and follow those loans through a 24-36 month period. Early payoffs, initial fees, and net charge offs should all be included in the determination of the yield on the portfolio.

Sound management requires routine review of each loan product. The review should determine that you are not

only meeting your member's needs but are also contributing to the overall success of the operation.

Loan Demand-

One of management's biggest challenges at present is stimulating consumer loan demand. Currently, the loan/share ratio for all Missouri credit unions is 78.5%. This is higher than the 71% of all federally insured credit unions in the U.S.; however, generating ample loan demand is still a burden. Building additional loan demand is key to producing solid earnings and improving net worth as well as serving the membership.

To meet/beat the competition and stimulate loan growth, each credit union needs to review the efficiency and effectiveness of the loan granting process.

1) Member Information

At one point in time, most credit unions verified the member's pay stub and calculated debt/income ratios (DIR) to determine the member's credit worthiness. However, with the use of credit scores to predict the member's potential to repay the loan, credit unions have generally moved away from income verification and DIR's and have moved toward a faster, more efficient method of predicting repayment. If you are still verifying income or calculating debt/income ratios, you may wish to review your approval process. Generally, a quick review of the member's credit report and determination of the credit score enables the loan officer to provide the member an immediate answer to the loan application. Providing the member with a rapid response generally stimulates member applications and hopefully generates additional loan volume.

2) Risk Based Pricing

How do you compete with dealer financing? Member education is definitely a key. However, it is undoubtedly a difficult task to convince the member that you can, in fact, beat the competition.

Pricing the loan based on risk may assist in closing the loan. Not only does this method permit the credit union to serve the weaker credit quality but also it rewards the member with a strong credit history. Rather than 'risk based pricing', you may want to take the approach of 'performance based pricing.' Members should be aware that a positive credit history is rewarded with favorable pricing.

3) Know Your Members

Each field of membership has its own personality. Identifying those items for which your members will go into debt is imperative to funding loan demand. Be creative --- modify maturities, look at different types of collateral, review pricing. Think 'out of the box' to grab

your member's attention and promote loan growth.

Stimulating loan growth requires an efficient, effective loan approval process. Quick turn-around, easy access, as well as reasonable pricing are all components of good lending.

FIELD OF MEMBERSHIP UP DATE

Springfield Telephone Employees Credit Union (now **Telcomm Credit Union**) submitted an application to include those persons who reside or work in the 417 telephone Area Code and the 573 (bordered on the north by I-70) telephone Area Code. The Director approved the expansion of **Springfield Telephone Employees Credit Union** to those in the 417 Area Code, but not the 573 Area Code. The decision was published in the November 15, 2000 Missouri Register. On November 30, 2000 the Missouri Bankers Association (MBA) and Century Bank of the Ozarks (CBO) filed an appeal of the decision to the Credit Union Commission. The Commission heard the appeal on March 29, 2001. On May 24, 2001 the Commission upheld the decision of the Director. On August 16, 2001, the decision was released and the Director filed **Springfield Telephone Employees Credit Union's** amended bylaws with the Secretary of State. On September 14, 2001, the MBA and CBO filed a petition for administrative review in Cole County Circuit Court.

On November 19, 2001, a hearing was held before Judge Tom Brown, Division 1, Circuit Court of Cole County. The motion to refer the case to another division of the court was granted and the case was referred to Judge Byron Kinder, Division 2. A motion to dismiss the case for lack of standing was heard on January 3, 2002. On January 29, 2002 the court ruled the plaintiffs lack standing to maintain causes of action set forth in their petition and ordered the plaintiffs' petition be dismissed. On March 11, 2002 the MBA and CBO filed an appeal of the decision in the Western Appellate Court of Appeals. Appellant's briefs were due June 3, 2002 with the respondent's briefs due July 3, 2002. A hearing by the Western Appellate Court was held on October 3, 2002 in Kansas City. On January 14, 2003, the Appellate Court upheld the decision of Cole County Circuit Court. On January 14, 2003, the MBA and CBO filed motions for a rehearing and transfer to the Missouri Supreme Court. The Appellate Court on March 4, 2003 denied the motions. On April 23, 2003, the Missouri Supreme Court issued an order transferring the case to their jurisdiction. On December 9, 2003 the Court reversed the decision of the lower courts and remanded the case. The opinion can be read at

<http://www.osca.state.mo.us/Courts/PubOpinions.nsf/0f87ea4ac0ad4c0186256405005d3b8e/d1c9a3590b16be4286256df6006dbc43?OpenDocument>. A status hearing has been scheduled for May 24, 2004 in Cole County Circuit

Court.

South Community Credit Union submitted an application for those who work or reside in Zip Codes 63109, 63111, 63116, 63123, 63125, 63128, 63129, and Crawford County, Franklin County, Gasconade County and Washington County. **Central Communications Credit Union** submitted an application for those persons who reside or work in the 816 telephone Area Code. The Director approved the applications submitted by **South Community and Central Communications Credit Unions**. These decisions were published in the November 15, 2000 Missouri Register. On November 30, 2000 the MBA and two local banks located in each of the two applicants' field of membership expansion areas filed appeals of the decisions to the Credit Union Commission. The Commission received the record of appeals from all parties on May 24, 2001. On August 9, 2001, the Commission upheld the decisions of the Director. The written decisions were released on January 25, 2002. On February 21, 2002, the MBA and the local banks filed a petition for administrative review in Cole County Circuit Court. Both cases were assigned to Judge Tom Brown, Division 1. On April 17, 2002 the cases were reassigned to Judge Byron L. Kinder, Division 2 and a motion was entered to stay the proceedings until the outcome of the Springfield Telephone Employees case was decided. The cases can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; the case numbers are 02CV323402 and 02CV323401. A status hearing has been scheduled for May 24, 2004 in Cole County Circuit Court.

Vantage Credit Union (formerly **Educational Employees Credit Union**) submitted an application for those who live or work in St. Louis County, St. Charles County, Jefferson County, Cape Girardeau County and Franklin County. The application was published in the December 15, 2000 Missouri Register. The Director approved the application and his decision was published in the February 15, 2001 Missouri Register. On March 1, 2001 the MBA and two banks located in the applicant's field of membership expansion area filed an appeal of the decision to the Credit Union Commission. The Commission received the record of appeal of **Educational Employees Credit Union** on October 19, 2001 and established briefing schedules. On March 5, 2002, the Commission dismissed the appeal due to lack of standing. On July 18, 2002 the MBA and the two banks filed a Petition in Mandamus in Cole County Circuit Court. On March 18, 2004 a mandamus order was issued and served on the Credit Union Commission. The case can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; case number 02CV324797.

City Utilities Credit Union submitted an application for community residents and workers in Greene and Christian

Counties. The application was published in the June 1, 2001 Missouri Register. The Director approved the application and his decision was published in the August 1, 2001 Missouri Register. On August 14, 2001 the MBA and a local bank located within the applicant's field of membership expansion area filed an appeal of the decision to the Credit Union Commission. On August 8, 2002 the Commission heard and denied the appeal for lack of standing. The decision was released on December 9, 2002. On January 2, 2003, MBA and the local bank filed a Petition in Mandamus in Cole County Circuit Court. On March 24, 2003 a status review and or trial setting was scheduled for May 24, 2004 in Cole County Circuit Court. The case can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; case number 03CV323001.

First Community Credit Union submitted an application for individuals who reside or work in the counties of Lincoln, Warren, Franklin, Washington, St. Francois, Ste. Genevieve, Pike, Montgomery, Gasconade and Crawford in the state of Missouri and the City of St. Louis. The application was published in the August 1, 2002 Missouri Register. The Director approved the application and his decision was published in the September 16, 2002 Missouri Register. On September 26, 2002 the MBA and a local bank located within the field of membership expansion area filed an appeal of the decision to the Credit Union Commission. On November 19, 2003 the Commission heard the appeal. On January 13, 2004 the Commission upheld the decision of the Director. The written decision was released on February 25, 2004. On March 19, 2004 the MBA and a local bank filed a petition for administrative review in Cole County Circuit Court. The case can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; case number 04CV323859.

Alliance Credit Union submitted an application for those who work or reside in St. Charles County or St. Louis County. The application was published in the November 15, 2002 Missouri Register. The Director approved the application and his decision was published in the January 16, 2003 Missouri Register. On January 30, 2003, the MBA and Allegiant Bank filed an appeal of the Director's decision with the Credit Union Commission. On November 19, 2003 the Commission heard the appeal. On January 13, 2004 the Commission upheld the decision of the Director. The written decision was released on February 25, 2004. On March 19, 2004 the MBA and a local bank filed a petition for administrative review in Cole County Circuit Court. The case can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; case number 04CV323857.

St. Louis Postal Credit Union submitted an application for those who live or work in the Zip Codes 63005, 63017, 63042, 63043, 63044, 63126, 63127 and St. Charles

County. The application was published in the December 2, 2002 Missouri Register. The director approved the application and his decision was published in the January 16, 2003 Missouri Register. On January 30, 2003, the MBA and Midwest Bank Centre filed an appeal of the Director's decision with the Credit Union Commission. On November 19, 2003 the Commission heard the appeal. On January 13, 2004 the Commission upheld the decision of the Director. The written decision was released on February 25, 2004. On March 19, 2004 the MBA and the local bank filed a petition for administrative review in Cole County Circuit Court. The case can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; case number 04CV323855.

United Community Credit Union, an Illinois chartered credit union, submitted an application for those who live or work in the Missouri counties of Lewis, Ralls and Marion. The application was published in the January 2, 2003 Missouri Register. The director approved the application and his decision was published in the February 18, 2003 Missouri Register. On March 4, 2003 the MBA and the Farmers and Merchants Bank and Trust Company filed an appeal of the Director's decision with the Credit Union Commission. On November 19, 2003 the Commission heard the appeal. On January 13, 2004 the Commission upheld the decision of the Director. The written decision was released on February 25, 2004. On March 19, 2004 the MBA and the local bank filed a petition for administrative review in Cole County Circuit Court. The case can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; case number 04CV323858.

Aerospace Community Credit Union submitted an application for those who live or work in the remainder of St. Louis City, St. Louis County and St. Charles County that is not currently in the **Aerospace Community Credit Union's** field of membership and those who live or work in Lincoln County. The application was published in the May 1, 2003 Missouri Register. The director approved the application and his decision was published in the July 1, 2003 Missouri Register. On July 14, 2003 the MBA and the First National Bank of St. Louis filed an appeal of the Director's decision with the Credit Union Commission. On November 19, 2003 the Commission heard the appeal. On January 13, 2004 the Commission upheld the decision of the Director. The written decision was released on February 25, 2004. On March 19, 2004 the MBA and the local bank filed a petition for administrative review in Cole County Circuit Court. The case can be followed on the internet at <http://casenet.osca.state.mo.us/casenet/>; case number 04CV323852.

Midwest United Credit Union submitted an application for all eligible businesses, government entities, individuals and the immediate family of all eligible individuals who live or work in Platte County, Missouri. The Director approved

these applications and his decision was published in the April 1, 2004 Missouri Register. On April 14, 2004, MBA and Platte Valley State Bank filed an appeal of the Director's decision with the Credit Union Commission. The Commission will schedule the appeal for hearing.

Edison Credit Union submitted an application for active or retired employees of Tenneco Automotive, Yates Electric Co. Inc., Trailmobile Cash Register Sales, Martec Pharmaceutical, Inc., Martec Scientific, Inc., Carlson Systems, and Reliable Health Care. **Goetz Credit Union** submitted an application for those who live or work in Buchanan County, Missouri. The Director approved these applications and his decisions were published in the April 1, 2004 Missouri Register. These decisions are now final.

Health Care Family Credit Union submitted an application for persons and families of persons who reside in or are employed in the 63143 Zip Code, a low-income area. The application was published in the April 15, 2004 Missouri Register. A ten business day comment period must occur before the Director can make a decision.

Clay County Teachers Credit Union submitted an application to include those who reside or work in Platte County, Missouri. **Century Credit Union** submitted an application to include persons working or residing in Jefferson County, Missouri. The applications will be published in the May 17, 2004 Missouri Register. A ten business day comment period must occur before the Director can make a decision.

From the Director...

Updated web site...

Links to credit union related internet sites have been added to the Division of Credit Unions site <http://www.ded.mo.gov/regulatorylicensing/creditunion/>. Our web site is a gateway to laws, forms, bulletins, newsletters, and research relating to credit unions.

Field of membership expansions...

If expansion of the credit union's field of membership would benefit the members of a credit union, an application should be submitted.



John P. Smith, Director

It was once said that the moral test of government is how that government treats those who are in the dawn of life, the children; those who are in the twilight of life, the elderly; and those who are in the shadows of life – the sick, the needy and

the handicapped.

-Senator Hubert H. Humphrey
